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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, DC 20554

In the Matter of	)	
	)	
2000 Biennial Regulatory Review—	)	
	)	**CC Docket No. 00-**
199		
Comprehensive Review of the Accounting Requirements and ARMIS Reporting Requirements for Incumbent Local Exchange Carriers: Phase 2 and Phase 3.	)	**(FCC 00-364)**

INITIAL COMMENTS OF THE
NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS

Pursuant to Sections 1.49, 1.415, and 1.419 of the Federal Communications Commission's ("FCC" or "Commission") Rules of Practice and Procedures, 47 C.F.R. Section 1.49, 1.415, and 1.419 (2000), the National Association of Regulatory Commissioners ("NARUC") respectfully submits these comments on the FCC's Notice of Proposed Rulemaking ("NPRM") adopted October 12, 2000, and released October 18, 2000 [FCC 00-364]. As discussed in more detail, *infra*, NARUC generally opposes many of the proposals suggested by the industry and put out for comment as part of this NPRM. In support of these positions, NARUC states as follows:

I. NARUC'S INTEREST

NARUC is a quasi-governmental nonprofit organization founded in 1889. Members include the governmental bodies engaged in the regulation of carriers and utilities from all fifty States, the District of Columbia, Puerto Rico, and the Virgin Islands. Those state and territorial officials are charged with regulating the telecommunications common carriers within their respective borders. They have a statutory obligation to assure that such telecommunications services and facilities as are

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required by the public convenience and necessity are established, and that services are furnished at rates that are just and reasonable.

Because of the potential impact on state commission procedures, and NARUC's stated goal of promoting more efficient regulation, NARUC has an interest in this proceeding.

NARUC applauds the efforts of the FCC staff to involve the states in this streamlining process, and respectfully suggests that the cooperative effort has been of mutual benefit.

Additionally, NARUC recognizes that the unique concerns individual states may have with the NPRM may vary. For this reason, we have urged the states to submit comments in this proceeding as well.[1]

II. BACKGROUND

In 1999, the FCC initiated a two-phased comprehensive review of its accounting rules and the related reporting requirements for incumbent local exchange carriers ("ILECs") to keep pace with changing conditions in a competitive telecommunications industry. In its Report and Order in CC Docket No. 99-253, ("Phase 1 Report and Order"), adopted on March 2, 2000 and released March 8, 2000, the FCC adopted accounting rule changes and reporting reform measures for the Automated Reporting Management Information System ("ARMIS").

In this current NPRM, the FCC initiates Phase 2 and Phase 3 of the comprehensive review of its accounting rules and reporting requirements. The NPRM seeks comment regarding FCC proposals to further streamline accounting and reporting requirements in the near-term (Phase 2) and the long-term (Phase 3) as the

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[1] *At its Annual Convention held November 11, 2000 in San Diego, California, NARUC adopted a resolution encouraging the FCC to continue to incorporate the input of the states in this instant and on-going proceedings involving the review of the FCC's accounting, cost allocation, and reporting rules. The resolution also encouraged states to file comments in this proceeding expressing their individual concerns and views. A copy of that resolution is attached to these comments as Appendix A.*

telecommunications industry moves towards a more competitive environment. The proposals for Phase 2 would eliminate one-fourth of the Class A accounts in the FCC's Uniform System of Accounts ("USOA"), 47 C.F.R. Part 32, the FCC's affiliate transaction rules, and the expense limits rules. The FCC's streamlining proposals for the largest ILECs generally encompass the elimination of 77 of 296 Class A accounts and elimination of related accounting aspects of ARMIS and data that are considered less useful and/or obsolete in a competitive environment.

Additionally, the NPRM seeks comment regarding whether the FCC should adopt the United States Telephone Association's ("USTA") proposal to further streamline the accounting and ARMIS requirements by eliminating Class A accounting altogether, eliminating the continuing property records ("CPR") requirements, eliminating forecasts for use in allocating joint costs between regulated and nonregulated activities, and eliminating the majority of the ARMIS reports including all state-by-state reporting requirements. Moreover, the NPRM seeks comment regarding whether certain accounts suggested by states should be added to reflect recent changes in technologies and regulatory requirements.

III. DISCUSSION

NARUC appreciates the opportunity to offer comments on this NPRM. *In general, the NARUC applauds the FCC's efforts to simplify and streamline its accounting and reporting requirements and certainly agrees with the elimination of any overlap of federal and state reporting requirements, as well as elimination of unnecessary reporting requirements.* However, because of the importance of these issues to the states, we have several concerns that are set forth in our comments below.

Our overall concern is that the Commission not act in a manner that would create a void in the FCC's and states' ability to obtain and rely on accurate information concerning costs and investments by the ILECs. Particularly, NARUC cautions that the impact of new technology, changes in the network infrastructure, and changes in the marketplace for telecommunications services, warrant reforms that are conducive, not counter, to the goals of a competitive local exchange market. Of greatest concern to the states is that deregulatory measures, such as eliminating accounting and reporting requirements for the ILECs, not be implemented in a wholesale manner. There has been rapid growth in internet traffic, packet switches, digital subscriber lines, and other services such as unbundled network elements ("UNEs") that place increasing reliance on the ILEC's network. At the same time, many of these ILECs have recently increased their operating areas through mergers and acquisitions. New competitors are attempting to compete in these markets, however the local exchange markets are not highly competitive. While it is important for the FCC to continue to streamline and reduce burdens on the ILECs as the local exchange market transitions to a competitive market, the need to monitor ILECs costs, investments, and cost allocation practices at this time is also important. *If ILECs can strategically shift costs and recover costs without regulatory oversight, both competition and consumers will be harmed.*

The states rely to a great deal on the FCC's Part 32 accounting system and on the information reported in ARMIS.[2] As the FCC moves forward with its efforts to deregulate and streamline its regulatory requirements, the NARUC urges the FCC to weigh in the balance the importance of ILECs' costs and practices on policies that could have a direct effect on competition and on the prices that consumers pay. Our specific concerns are addressed below.

1. Elimination of account details is premature:

NARUC believes that the proposed elimination of operations, corporate, and administrative expense account details may cause problems for states that use such data

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[2]Recently, the Federal-State Joint Board on Separations adopted a Recommended Decision to freeze separations factors as efforts to bring about comprehensive reform to jurisdictional separations rules continue. See *Jurisdictional Separations Reform and Referral to the Federal-State Joint Board,* CC Docket No. 80-286, Recommended Decision, FCC 00J-2, 15 FCC Rcd 13160 (2000). This Recommended Decision, which sets out concerns about cost shifting and the need to prevent recovery of the same costs in both interstate and intrastate jurisdictions, notes that Part 32 is the first step in establishing appropriate interstate and intrastate rates. Id. at para. 4.

in tariffing and UNE pricing functions. In addition, we find the USTA's proposals to eliminate Class A accounting requirements are also problematic. The loss of the detail provided in Class A accounting requirements would undermine the states' ability to understand the nature of the carriers' costs. The carriers' costs are largely driven by their network plant investments. Under Class B accounting, almost nothing would be known about these costs. For example, under Class B accounting, all outside cable and wire investments are contained in one account. No detail would be available regarding the construction or makeup of the various types of outside plant. All fiber, copper, aerial, underground, and buried cables as well as poles and conduit would be combined together in one account. These separate accounts are critical cost components used to establish proper universal service support, UNE, pole attachment, and other rates that ILECs charge its customers and competitors. States rely on the data that carriers report to the FCC and this separate account information is often used by the states and others in support of such pricing decisions.

NARUC also believes that the lack of detailed cost data would undermine the states' ability to set or assess the carriers' depreciation rates or even the FCC's life and salvage ranges. This is because the various types of plant inherently have widely diverse life and salvage characteristics. Combining them together would seriously distort the usefulness of the current prescribed FCC ranges and undermine all the programs that rely on them (i.e., universal service cost proxy models, UNE pricing, etc.). Moreover, no cost data would be available for the FCC or the states to develop realistic cost models or even evaluate cost studies prepared by the carriers.

NARUC finds the USTA's argument that Class A accounting requirements are too burdensome for the largest ILECs makes little sense considering these carriers maintain from 2,000 to 3,500 accounts in their own accounting systems. When complying with the FCC's current Class A accounting, the carriers simply aggregate their own account balances into the Class A format, that consists of approximately 300 accounts. Also, the smallest ILECs use Class A accounting, a requirement for acquiring Rural Utility Service ("RUS") loans.

2. *Some additional accounts are needed:*

The accounts suggested by states for new technologies are appropriate and necessary to enable the FCC to maintain an up-to-date accounting system. These accounts will enable the FCC and states to continue to understand the nature of the carrier's investment and ensure that prices are reflective of their actual costs. Moreover, such information will enable the FCC and states to monitor issues such as deployment, collocation, and interconnection cooperation. The creation of expense and revenue accounts for UNE and interconnection will help states administer the prices of these services.

3. *Elimination of Continuing Property Records (CPR) is premature:*

NARUC believes that the USTA's proposal to eliminate existing CPR requirements is also problematic. These records are necessary to ensure that the largest and most important accounts, the network plant accounts, accurately reflect those assets actually in service. Also, CPRs provide data for jurisdictional separations and cost allocations studies. Moreover, these records provide material-only costs for accounting for transfers, reallocations, and adjustments of plant. If these records are inaccurate, virtually all of the carriers' cost data becomes suspect. Furthermore, CPR discrepancies could have an impact on current levels of universal support since the existing methodology calculates support based on historical financial information. On a forward-looking basis, interstate universal service support for nonrural ILECs may be affected, to the extent that the proxy model employed utilized historical relationships to determine forward-looking plant specific expense and other expense categories. NARUC notes that the FCC recently directed the staff of the Common Carrier Bureau and the carriers to clean up these records and accounts.

4. Elimination of the Forecast Use Rule for allocating joint costs is premature:

Additionally, the NARUC believes that eliminating the forecast use rule for allocating joint investments between the carriers' regulated operations and nonregulated 'upstart' (or new) operations would result in the over allocation of nonregulated costs to the carriers' regulated operation. The markets for carriers' regulated activities are large, well-established, and mature, while the nonregulated activities, subject to the 'forecast use' rule, are new 'upstart' activities, in their infancy. These new upstart activities are generally activities where the potential for robust competition is greatest. If ILECs have the ability to shift the costs of these new service offerings to their regulated activities, competition for these new upstart services will be seriously undermined. The forecast use rule, which is based on the cost causative principle, is critical for allocating costs fairly because forecasted use provides the best measure of the new services' intended use. As carriers make investments aimed at increasing their revenues in new 'upstart' nonregulated activities it is important to use forecasts so that the FCC can allocate the appropriate 'use' of the new assets to the carriers' nonregulated activities. Otherwise, the carriers could allocate almost all of the new investments to the regulated operations for many years even though the investments are primarily made to develop their newer, nonregulated activities.

5. Increasing the current expense limits is not warranted:

Regarding the USTA's proposal to increase the current expense limit, NARUC believes that circumstances have not changed significantly since 1997 to warrant a further increase in the current $2,000 expense limit or to extend the expense limit to all plant asset accounts. The exception would be tools and test equipment located in the central office that currently have a $500 expense limit. NARUC believes there is little difference between the tools and test equipment contained in the general support function and that equipment in the central office function to warrant different expense limits. Regardless of their physical location, these assets are virtually the same and should be subject to similar expense limits. For this reason, we believe the $2,000 expense limit should be extended to include central office tools and test equipment assets. On the other hand, the majority of the investment contained in the General Support Computer account is associated with personal computers and peripheral equipment costing less than $2,000 and, in many cases, less than $1,000. Increasing the expense limit for these assets to $2,000 would result in very little, if any, capitalization. Therefore, the NARUC does not believe the existing $500 expense limit should be increased to $2,000 for the computer assets.

6. No change in the 50 percent prevailing price threshold for valuing affiliate transactions is needed:

Another proposal by the USTA is that the FCC revise section 32.27(d) to decrease the threshold from 50 percent to 25 percent for use of prevailing price in valuing affiliate transactions. Under this proposal, an affiliate, such as a supply company, can conduct up to 75 percent of its business with the ILEC and charge prevailing price. Volume discounts or other cost savings which the affiliate experiences primarily due to its association with the ILEC will not have to be passed on to the ILEC. If over 50 percent of the affiliate's sales are to the ILEC, then it seems that the primary purpose of the affiliate is to serve the ILEC. The FCC's current threshold of 50 percent for use of prevailing price in valuing affiliate transactions recognizes that the affiliate exists to serve the ILEC. Therefore, the NARUC does not recommend or support any change in the 50 percent threshold.

7. Streamlined ARMIS Reporting Requirements:

The USTA's proposal to eliminate practically all current ARMIS reporting requirements for mid-sized carriers is particularly troublesome.[3] All of the ARMIS reports are important to understand the carriers' local exchange and access operations,

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[3] NARUC notes that these reduced reporting requirements, in combination with the lower quality of service reporting requirements anticipated in FCC Docket No. 00-229, may result in an unwarranted lessening of requirements on the ILECs. At this time, NARUC is not convinced that the ILECs have "earned" such a reduced level of reporting nor that the ILECs' conduct regarding competition is evidence of a lessening need for the data.

both financially and technically. The FCC's statutory mandate is to assure a rapid and efficient nationwide telecommunications system to all Americans. The states have other responsibilities that in many ways mirror the FCC's responsibilities. Without certain basic information, the FCC and the states will be hampered in carrying out their responsibilities. The FCC sets forth the basic information it will require from carriers in its accounting, service quality, and network infrastructure rules and orders. ARMIS makes this basic information public. ARMIS reporting does not present a significant burden to the carriers. ARMIS only requires carriers to provide information on certain data otherwise required by FCC rules and does not make public any proprietary data. Additionally, ARMIS data is collected in a uniform and standard format so that the states and the public have efficient and reliable access to critical data that is needed in establishing regulated service rates, UNE prices, interconnection rates, depreciation rates, universal service support, assessing service quality, and service quality trends, network functionality, capabilities, and reliability.

Further, NARUC believes the USTA's proposal to eliminate state-by-state ARMIS information would undermine the states' ability to use any data provided in ARMIS. Moreover, it would harm the FCC's ability to monitor and investigate ILEC activities, especially in cases where a targeted investigation may be warranted.[4] ARMIS was designed to accommodate both FCC and state needs. To eliminate the information provided on a state basis would undermine the goals that ARMIS sought to achieve. The carriers are required by most states to maintain this data on a state basis. Thus, no burden is placed on the carrier to maintain the state data, and the burden to report it is minimal.

On the other hand, NARUC fully supports the FCC's proposal to eliminate the collection of obsolete data and to update its ARMIS reports to obtain information on new

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[4] The Ameritech service quality issue is a good example where target investigation may be warranted as a result of the data reported in ARMIS. See *October 6, 2000 letter to James Calloway, Group President - SBC Services from Dorothy Attwood, Chief, Common Carrier Bureau*, FCC, DA 00-2298, regarding the downward trend in service quality based on quarterly reports filed with the FCC pursuant to the Merger Conditions.

technologies (upgrades and investments in switching and transmission capacity) that are critical components of the carrier's network infrastructure. The information that the FCC proposes to collect is basic to the FCC's responsibilities to assure the integrity of the country's network and should impose minimal burden on the carriers. The elimination of data (approximately half of what is collected today) will further ease the data collection burden on the carrier.

8. Relief for Mid-Sized ILECs:

Additionally, in its Accounting Reductions Report and Order in CC Docket No. 98-11 and its ARMIS Reductions Report and Order in CC Docket No. 98-117, both adopted May 18, 1999 and released June 30, 1999, the FCC reduced accounting and reporting requirements for mid-size ILECs by allowing them to report on a Class B level. These streamlining measures along with the additional Class A reporting reform measures and the proposed increase in the revenue threshold to $200 million proposed in the instant NPRM appear to be more than adequate relief measures for mid-size ILECs at this time. The NARUC does not believe any further reporting relief is needed.

IV. CONCLUSION

In conclusion, while the NARUC applauds the FCC's continued efforts to streamline accounting and reporting requirements in line with the telecommunications changing environment, we take issue with several of the USTA proposals:

First, the proposal to eliminate Class A accounting requirements will result in a lack of detailed data for accounts that comprise the major portion of an ILEC's investment (outside plant cable accounts, switching, and circuit). This will, in turn, make it more onerous for states in analyzing and evaluating ILEC cost studies prepared for determining universal support, UNE prices, and interconnection prices.

Second, we do not support the proposals regarding cost allocations, affiliate transactions, expense limits, and continuing property records requirements. The forecast use rule is critical for allocating costs fairly between the ILECs' regulated operations and the nonregulated 'startup' operations because it is based on the cost causative principle. Elimination of this rule could result in the ILEC allocating virtually all of the new investments to the regulated operations even though the investments are being made primarily to develop the new, nonregulated activities.

Additionally, we believe the FCC's current 50 percent threshold for use of prevailing price in valuing affiliate transactions recognizes that the affiliate exists to serve the ILEC. Accordingly, a decrease in the threshold makes little sense.

As for the existing $2,000 expense limit for certain general support assets, we believe circumstances have not significantly changed since 1997 to warrant an increase. On the other hand, there is little difference between the tools and test equipment contained in the general support function and that equipment in the central office function to warrant different expense limits. In contrast, the assets comprising the General Support Computer account, in many cases, cost less than $1,000 indicating that an increase in the $500 threshold would essentially eliminate the account.

Regarding the elimination of CPR requirements, inaccurate CPRs could have an impact on current levels of universal support since the existing methodology calculates support based on historical financial information. On a forward-looking basis, interstate universal service support for nonrural ILECs may be affected, if the proxy model utilizes historical relationships to determine forward-looking expenses.

Finally, the USTA's proposals to eliminate practically all current reporting requirements would seriously inhibit the states' use of any data provided in ARMIS. This information represents our only publicly available source of accounting data and information utilized in establishing UNE prices, interconnection rates, universal service support; and, assessing service quality trends and network functionality, capabilities, and reliability.

For the mid-sized ILECs, NARUC believes that the reduced accounting and reporting requirements made in the Accounting Reductions Report and Order and the ARMIS Reductions Report and Order, along with the additional Class A reporting reform measures and the proposed increase in the revenue threshold to $200 million, appear to be more than adequate relief measures for mid-sized ILECs at this time.

Finally, NARUC supports the FCC's proposal to eliminate the collection of obsolete data and to update its ARMIS reports to obtain information on new technologies that are critical components of the ILEC's network infrastructure. The proposal will eliminate approximately half the data collected today and will further ease the data collection burden on the ILEC.

For the forgoing reasons, NARUC respectfully requests that the FCC carefully consider and implement the positions outlined in these comments.

Respectfully Submitted,

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DECEMBER 21, 2000

APPENDIX A

Resolution Urging Regulatory Jurisdictions to Comment on the Federal Communication Commission's Comprehensive Review of the Accounting Requirements and ARMIS Reporting Requirements for Incumbent Local Exchange Carriers

WHEREAS, On October 12, 2000, the Federal Communications Commission ("FCC") adopted a Notice of Proposed Rulemaking ("NPRM") in Phase 2 and Phase 3 of its comprehensive review of Part 32 accounting rules and ARMIS reporting requirements*; and*

WHEREAS, The NPRM contains various proposals, including: USTA's proposal to streamline the accounting system for large carries to the Class B level of accounts; a proposal to streamline the accounting system that maintains the Class A level of detail for plant and plant expense accounts; state proposals for revising the chart of accounts*; and* other proposals calling for revisions to the FCC's Part 32 accounting rules and ARMIS reporting requirements, including modifications to the affiliate transactions rules and the accounting rules and reporting requirements for mid-sized carriers*; and*

WHEREAS, The FCC staff and staff representatives from numerous state utility commissions worked as a team to provide input to the formulation and development of this rulemaking process through conference calls and public meetings to discuss the accounting issues;

WHEREAS, The data recorded in the Uniform System of Accounts ("USOA") and reported in ARMIS by the larger and mid-sized carriers are essential for many purposes including: evaluating unbundled network element, access, and local rates; monitoring quality of service; calculating federal and state universal service support; evaluating the competitive nature of the telecommunications market; and performing benchmarking analyses;

WHEREAS, The data recorded in the USOA or reported in ARMIS can also provide important information to the states and territories regarding the deployment of and cost of new technologies and services*; and*

WHEREAS, The states and territories generally adopted the current Part 32 accounting rules by reference to simplify regulatory burdens and to provide consistency of multi-jurisdictional data*; and*

WHEREAS, The states generally find that accounting safeguards are essential for monitoring and implementing the competitive mandates and cross-subsidy prohibitions of the 1996 Telecommunications Act*; and*

WHEREAS, At its 1999 Winter meetings in Washington, D.C., NARUC adopted a resolution stating the importance of the ARMIS data to its members and urging the FCC to solicit inputs from the states and territories prior to implementing significant changes to the ARMIS reporting requirements; *now therefore be it*

RESOLVED, That the National Association of Regulatory Utility Commissioners (NARUC), assembled in its November 2000 112th Annual Meeting in San Diego, California, commends the

FCC for seeking and gathering input from the states early in the process of formulating the issues in this proceeding and encourages the FCC to continue to incorporate the input of the states and territories in this and on-going proceedings involving the review of the FCC's accounting, cost allocation, and reporting rules, *and be it further*

RESOLVED, That the states and territories are encouraged to file comments in the FCC's proceeding in CC Docket No. 00-199, responding to the FCC's request for comments on a variety of reporting and accounting issues, including:

- How the FCC's accounting rules and ARMIS data are used in state and territory proceedings such as unbundled network element or other intrastate ratemaking;
- How federal and state universal service funds are or are likely to be affected by the proposed changes to the rules;
- The importance, if any, of the accounting and reporting rules for the separations process;
- Is the accounting data necessary and how is it used, if at all, to assess the development of competition in the local exchange telecommunications market;
- What level of accounting and reporting disaggregation is necessary to support state and territory policymaking initiatives;
- How USTA's proposal to streamline the accounting system for large carriers to the Call B level of accounts would affect state and territory proceedings that rely on the FCC's accounting rules and ARMIS data;
- Any other matters in which the states or territories use the FCC's accounting data or in which the states or territories would need additional Part 32 accounts*; and*
- How a roadmap for accounting deregulation could and should be developed at the federal level.

Sponsored by the Committee on Finance and Technology.
Recommended by the Board of Directors.
Adopted in Convention November 15, 2000.